

## Summary of Public Chapter 982

Franchise,  
Excise  
taxes  
notice

**CHAPTER 982**  
**OF THE PUBLIC ACTS OF 2000**  
**Senate Bill 3082     House Bill 3010**

**TECHNICAL CORRECTIONS BILL**

**SECTION-BY-SECTION  
SUMMARY**

The following is an abbreviated summary of Chapter 982 of the Public acts of 2000 known as the “Technical Corrections Bill.” It has been prepared by the Department of Revenue’s Legal Office in response to requests for a further explanation the provisions of the Act. The language used is not quoted verbatim from the Act and should not be used as a substitute for the formal text of the law. The Administration or the Commissioner may make further determinations with regard to application and administration of the Act.

**SECTION 1.** Franchise and excise tax: Removes the word “corporation” from the financial institution statutes and replaces it with the word “person” to comply with definition of a “taxpayer” or “person.” This enables any business entity subject to franchise, excise taxes (limited partnerships, limited liability companies, etc.) to be classified as a financial institution if it otherwise meets the statutory criteria.

**SECTION 2.** Franchise and excise tax: Defines “compensation” for apportionment purposes as it was before enactment of 1999 PC 406. This was necessary since the definition in PC 406 was designed to address compensation that would have been included in the excise tax base under proposed legislation that never became law.

**SECTION 3.** Franchise and excise tax: Defines “general partnership.” General partnerships are not subject to franchise, excise taxes and are defined as partnerships in which all partners are fully liable for the debts of the partnership even though claims against a partner may be limited by contract.

**SECTION 4.** Franchise and excise tax: Clarifies that “gross receipts,” “total gross receipts,” “total receipts” and “receipts” all to have the same meaning.

**SECTION 5.** Franchise and excise tax: Broadens the definition of “not-for-profit” so that certain additional entities which are exempt from federal income tax are also exempt from the Tennessee tax.

**SECTION 6.** Franchise and excise tax: Eliminates the phrase “and any other organization or entity engaged in business” from the definition of a person subject to the tax. Under this definition, entities subject to franchise, excise taxes are limited to those named and are not

necessarily classified in accordance with IRC Section 7701.

**SECTION 7.** Franchise and excise tax: Deletes definitions pertaining to staff leasing. These definitions are not necessary under PC 406 because it does not require compensation to be included in the excise tax base, and thus it is not an issue for staff leasing companies.

**SECTION 8.** Excise tax: Makes clear that a limited liability company treated as a corporation for federal income tax purposes is taxed as a corporation for franchise, excise tax purposes.

**SECTION 9.** Excise tax: Eliminates unnecessary reference.

**SECTION 10.** Excise tax: Makes clear that capital gains are included in taxable net earnings of an entity treated as a partnership for federal tax purposes.

**SECTION 11.** Excise tax: Makes clear that deductible amounts subject to self-employment tax are not limited by any cap.

**SECTION 12.** Excise tax: Makes clear that estates, as such, are not subject to the excise tax. However, an estate conducting an ongoing business enterprise may be subject to franchise and excise taxes.

**SECTION 13.** Excise tax: Makes clear that a limited liability company, whose single member is a general partnership, is subject to excise tax.

**SECTION 14.** Excise tax: Permits an insurance company, that does not take an excise tax credit for gross premiums

taxes paid, to deduct such taxes in determining the excise tax base.

**SECTION 15.** Excise tax: Clarifies that exempt entities, that have income unrelated to the activities upon which the exemption is based, are subject to excise tax on such income.

**SECTION 16.** Excise tax: Makes clear that a taxpayer doing business in Tennessee is subject to tax even though the taxpayer may have failed to obtain a charter or certificate of authority, etc.

**SECTION 17.** Excise tax: Requires an entity to be classified as a corporation, partnership, or other entity in accordance with the way it is treated for federal income tax purposes, and makes clear that, except in the case of a limited liability company whose single member is a corporation and unitary groups permitted or required to file combined returns, each taxpayer is considered a separate entity and must file its return on that basis. Federal taxable income on a separate entity basis will be the same as would have been computed for federal purposes had the entity been filing its federal return on a separate entity basis.

**SECTION 18.** Franchise and excise tax: Provides for the following new exemptions:

- Venture capital funds that are LLCs, LLPs, or LPs and are formed and operated for the exclusive purpose of buying, holding and/or selling securities primarily in non-publicly traded companies on their own behalf and not as a broker, the capital of which fund is primarily derived from investments by entities

and/or individuals that are neither related to nor affiliated with the fund. For this purpose, the following applies:

“Related” is determined in accordance with IRC Section 267(b) and (f).

“Affiliated” means entities that are affiliated under in IRC Section 1504(a).

“Primarily” means over 50%.

“Non-publicly traded companies” is an entity that is not a “publicly traded company.”

“Publicly traded company” means a company traded on:

A national securities exchange registered under Section 6 of the Securities Exchange Act of 1934 or exempted from such registration because of limited volume.

A foreign exchange operating under principles analogous to a national securities exchange.

A regional or local exchange.

An interdealer quotation system that regularly disseminates, by electronic means or otherwise, firm buy or sell quotations by

identified brokers or dealers.

A secondary market or equivalent if the owners are readily able to buy, sell or exchange their ownership interest in a manner comparable economically to trading on an exchange.

- LLCs, LLPs and LPs who meet the following criteria:

Has at least 66.67% of its activities in either farming or the holding of personal residence(s) where one or more members or partners reside. For this purpose:

“Farming” is, for human or animal use or consumption, the growing of crops, nursery products, timber or fibers, or the keeping of horses, cattle, sheep, goats, chickens or other animals, or the keeping of animals that produce products such as milk, eggs, wool or hides.

To be considered farming, 66.67% of the entity’s income (including capital gains from the sale of farm assets, must be derived from farming, and 66.67% of its assets must be used by the owner, lessee or sharecropper for

farming. Property is to be valued at fair market value if original cost cannot be determined.

A “personal residence(s)” includes acreage contiguous to the dwelling.

If an entity qualifies for exemption at least 5 years due to farming or personal residence, the exemption shall continue for 1 year from the end of the calendar year in which it ceases to qualify for exemption but only with regard to transactions related to property held at the time it last qualified for exemption.

For a dwelling to qualify as a personal residence, partners or members must occupy it for personal use for more days than it is rented to others and “personal use” will be defined by IRC Section 280A(d)(2).

At least 95% of the voting rights, capital interest or profits must be owned by natural persons who are relatives or by trusts for their benefit. Natural persons are relatives if, by blood or adoption, they are descended from a common ancestor and

their relationship is that of a 1<sup>st</sup> cousin or closer or if they are spouses.

- LLCs, LLPs or LPs existing on 5-1-99 and who, on such date and at all times thereafter meet all of the following criteria:

Are at least 98% owned by corporate members of an affiliated group as defined by 26 U.S.C. Section 1504(a).

Were formed and operated exclusively to acquire notes, accounts receivable, installment sale contracts, and similar evidences of indebtedness from members of the affiliated group.

Assets of the entity serve, directly or indirectly, as security for 3<sup>rd</sup> party borrowings or securitized indebtedness acquired by third parties.

At least 80% of the income from such acquisitions is included in the income of a corporation doing business in Tennessee.

Such income is subject to allocation and apportionment.

- LLCs, LLPs, and LPs, all of whose members or partners are fully liable for the debts,

obligations and liabilities of the entity and who have filed appropriate documentation with the Secretary of State to that effect on or before the first day of the taxable year or, in the case of tax years beginning before 1-2-2000, before 9-15-2000. The statute sets forth extensive requirements and conditions to qualify for this exemption, which also includes certain real estate mortgage investment conduits and financial asset securitization investment trusts.

**SECTION 19.** Excise tax: Makes clear that, in order to claim an excise tax credit for the purchase of computers that do not fall within the sales tax definition of industrial machinery, the taxpayer must qualify for the job tax credit.

**SECTION 20.** Excise tax: Provides that a taxpayer's ownership share of Tennessee property, owned or used by certain entities not subject to the tax, shall be included in the property factor of the taxpayer's apportionment formula.

**SECTION 21.** Excise tax: Provides that a taxpayer's ownership share of Tennessee compensation of certain entities not subject to the tax shall be included in the payroll factor of the taxpayer's apportionment formula.

**SECTION 22.** Excise tax: Provides that a taxpayer's ownership share of Tennessee gross receipts of certain entities not subject to the tax shall be included in the gross receipts factor of the taxpayer's apportionment formula.

**SECTION 23.** Franchise and excise tax: Makes clear that quarterly payments must each be based on the tax liability for the entire base year, and clarifies that no quarterly payments are required if the current year's tax liability is less than \$5,000.

**SECTION 24.** Franchise and excise tax: Makes it clear that a taxpayer who timely makes quarterly payments, each of which equals 25% of its tax liability for the current year, will not incur a deficiency penalty.

**SECTION 25.** Franchise and excise tax: Lowers the payment required with an extension request from 100% to 90% of the current year's liability.

**SECTION 26.** Excise tax: Allows credits and loss carryforwards incurred by an entity doing business in Tennessee prior to being subject to franchise, excise taxes if the following criteria are met:

- The entity was formed after 12-31-95.
- The entity was not subject to franchise, excise taxes prior to the date Chapter 406 of the Public Acts of 1999 became applicable.
- Had it been subject to franchise, excise taxes, the entity could have qualified for the job tax credit and carryover thereof for the calendar tax years 1997 and 1998 under Tenn. Code Ann. Section 67-4-908(c) prior to its repeal.

Industrial machinery excise tax credits, job tax credits and loss carryovers must be computed as though the entity had been subject to excise tax for the tax years 1997 and 1998 and applied accordingly to year(s) subsequent to the year in which the credit or loss was incurred. Unused credits or losses, if any, may then be carried forward to years in which the entity is subject to franchise, excise taxes.

**SECTION 27.** Franchise tax: Clarifies that limited liability companies are subject to the tax regardless of how they are treated for federal income tax purposes. Defines unrelated business taxable income (loss) of an exempt entity in accordance with the Internal Revenue Code.

**SECTION 28.** Franchise tax: Makes clear that a taxpayer doing business in Tennessee is subject to tax even though such taxpayer may have failed to obtain a charter, domestication, qualification, certificate of authority, or registration or same has been forfeited, revoked or suspended.

**SECTION 29.** Franchise tax: Allows certain taxpayers who do not keep their books and records using generally accepted accounting principles to compute net worth using the method described in Section 30.

**SECTION 30.** Franchise tax: Allows taxpayers, except for unitary groups filing on a combined basis, who do not keep their books and records using generally accepted accounting principles, to compute net worth using the same method used for federal income tax purposes as long as such method fairly reflects the taxpayer's net worth

for purposes of the franchise tax. Net worth is defined as total assets less total liabilities.

**SECTION 31.** Franchise tax: Requires an entity to be classified as a corporation, partnership, or other entity in accordance with the way it is treated for federal income tax purposes, and makes clear that, except in the case of a limited liability company whose single member is a corporation and unitary groups permitted or required to file combined returns, each taxpayer is considered a separate entity and must file its return on that basis. Federal taxable income on a separate entity basis will be the same as would have been computed for federal purposes had the entity been filing its federal return on a separate entity basis.

**SECTION 32.** Franchise tax: Except for entities permitted or required to file combined returns as a unitary group, allows taxpayers to compute the value an interest in another taxpayer deductible from net worth in accordance with the method used for federal tax purposes if they do not keep their books and records using generally accepted accounting principles

**SECTION 33.** Franchise tax: Except for entities permitted or required to file combined returns as a unitary group, allows taxpayers, who do not keep their books and records using generally accepted accounting principles, to compute property owned or used for purposes of the franchise tax minimum measure in accordance with the method used for federal tax purposes as long as that method fairly reflects the value of the property.

Includes in the minimum measure property owned or rented by a general partnership in which the taxpayer is a partner. A limited liability company with a general partnership as its single member need only include in its minimum measure the real or tangible personal property that it owns or uses and may exclude that owned or used by its single member general partnership.

The taxpayer's minimum franchise tax measure must also include its ownership share of real and tangible property owned or used by a general or limited partnership, S corporation, LLC, or any other entity treated as a partnership for federal tax purposes and not subject to franchise, excise taxes.

**SECTION 34.** Franchise, excise tax: Amends job tax credit to make consistent with taxation of entities other than corporations. The amendment allows an entity subject to franchise, excise taxes to be a qualified business enterprise for purposes of the job tax credit if it invests in the creation or expansion of a Tennessee office, not just a corporate office.

**SECTION 35.** Franchise tax: Provides that a taxpayer's ownership share of Tennessee property owned or used by certain entities not subject to the tax shall be included in the property factor of the taxpayer's apportionment formula.

**SECTION 36.** Franchise tax: Provides that a taxpayer's ownership share of Tennessee compensation of certain entities not subject to the tax shall be included in the payroll factor of the taxpayer's apportionment formula.

**SECTION 37.** Franchise tax: Provides that a taxpayer's ownership share of Tennessee gross receipts of certain entities not subject to the tax shall be included in the gross receipts factor of the taxpayer's apportionment formula.

**SECTION 38.** Franchise tax: Makes clear that each entity incorporated, domesticated, qualified or otherwise registered to do business in Tennessee is subject to at least the minimum \$100 tax each year even if inactive or, without proper dissolution, has had its charter, domestication, qualification or registration forfeited, revoked or suspended.

**SECTION 39.** All taxes: For purposes of our confidentiality statutes, defines "tax administration information" as criteria, standards, or data used for audit selection purposes, audit procedures, or any other information related to tax administration.

**SECTION 40.** All taxes: Makes tax administration information confidential. Under prior law, such information usually did not qualify as a "return" or as "tax information" as defined in our confidentiality statutes and thus, was available on request under the open records statutes. This amendment prohibits disclosure of such information unless otherwise provided by our confidentiality statutes.

**SECTION 41.** All taxes: Makes it a class E felony for any employee of the Department of Revenue to willfully inspect any return or tax information except when the employee has a good faith and objectively reasonable basis for believing such inspection is in

furtherance of his or her duties or responsibilities.

**SECTION 42.** All taxes: Authorizes the Commissioner to disclose tax administration information if the Commissioner determines that it is in the best interest of the state to do so.

**SECTION 43.** Sales and use tax: Prohibits state and local government from contracting with any person unless the person's affiliates register for sales tax. The Commissioner may provide tax information to a state agency or state entity to insure compliance.

**SECTION 44.** Use tax: The offense of tax evasion is reduced to a Class A misdemeanor if use tax of less than \$500 is involved.

**SECTION 45.** Franchise and excise tax: Defines a "pass-through entity" as an S corporation or any entity treated as a partnership or trust for federal income tax purposes but that has a single owner and is disregarded as an entity separate from its owner for federal purposes but not for franchise, excise tax purposes. A "real estate investment trust" is defined as an entity that has made an IRC Section 856(c)(i) election.

**SECTION 46.** Excise tax: Requires any item of loss or expense from a pass-through entity subject to excise tax to be added to the entity's net earnings or losses if it has been included in the computation of such earnings or losses and is allocated to a partner, shareholder, beneficiary or owner.

It also requires any item of loss or expense of a pass-through entity subject to excise tax to be added to the entity's

net earnings or losses if it has been included in the federal taxable income or loss of a real estate investment trust that owns an interest in the pass-through entity either directly or indirectly through 1 or more such entities and which files an excise tax return.

The provisions of this Section and other Sections of the Act have the effect of exempting from the excise tax qualified subchapter S corporation subsidiaries (QSSSs) and partnerships (UP-REITs or umbrella partnerships) to the extent owned by S corporations or real estate investment trust companies subject to the excise tax. The amendments, in effect, throw the income or losses of such entities into the S corporation or real estate investment trust owner, and thus it is excise taxed in accordance with the statutes that apply to the S corporation or real estate investment trust.

Although the QSSS, UP-REIT, or entity that has a single owner may be disregarded for federal purposes and may file as one and the same with its single owner, it files separately for franchise, excise tax purposes (unless it is an LLC). But, to the extent that its income is effectively thrown into its excise taxed single owner, it is exempt from the excise tax under these provisions.

The income of such an entity would be in federal taxable income of the S corporation, REIT, or single member and is subject to excise tax. However, since a REIT may deduct dividends paid in determining its federal taxable income, if it pays out all its income, it has no excise tax base. Thus, the statutes give an UP-REIT the benefit of



the dividends paid deduction. Under federal law, REIT is required to pay out at least 95% of its earnings in dividends.

If an UP-REIT is not 100% owned by an excise taxable REIT, it would be subject to excise tax to the extent that it is owned by a REIT not subject to excise tax or a non-REIT entity. A QSSS is always 100% owned by an S corporation.

**SECTION 47:** Excise tax: Requires any item of net gain or income from a pass-through entity subject to excise tax to be deducted from the entity's net earnings or losses if it has been included in the computation of such earnings or losses and is allocated to a partner, shareholder, beneficiary or owner.

It also requires any item of net gain or income of a pass-through entity subject to excise tax to be deducted from the entity's net earnings or losses if it has been included in the federal taxable income or loss of a real estate investment trust that owns an interest in the pass-through entity either directly or indirectly through 1 or more such entities and which files an excise tax return.

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The income of such an entity would be in federal taxable income of the S corporation, REIT, or single member, and is subject to excise tax. However, since a REIT may deduct dividends paid in determining its federal taxable income, if it pays out all its income, it has no excise tax base. Thus, the statutes give an UP-REIT the benefit of the dividends paid deduction. Under federal law, REIT is required to pay out at least 95% of its earnings in dividends.

If an UP-REIT is not 100% owned by an excise taxable REIT, it would be subject to excise tax to the extent that it is owned by a REIT not subject to excise tax or a non-REIT entity. A QSSS is always 100% owned by an S corporation.

**SECTION 48:** Excise tax: Requires property, payroll and receipts from of a pass-through entity to be included in a taxpayer's apportionment formula in the same proportion by which the taxpayer shares federal taxable income or losses of the pass-through entity if such items were not excluded in computing taxable

income or loss of the pass-through entity.

**SECTION 49:** Franchise tax: This amendment is necessary to reflect the franchise tax exemption for entities 100% owned by REITs which is contained in Section 50.

**SECTION 50:** Franchise tax: Provides an exemption from the franchise tax for an entity treated as a partnership for federal tax purposes when it is, directly or indirectly, 100% owned by a REIT.

If the entity is only partly owned by a REIT, it must file as though not exempt and multiply its franchise tax by the percentage of ownership by non-REITs to determine its franchise tax liability.

**SECTION 51:** Franchise tax: Permits an entity treated as a partnership for federal tax purposes (excluding S corporations) and in which a REIT directly or indirectly owns a majority interest in capital and profits to use net worth as the sole measure of its franchise tax.

**SECTION 52.** Franchise tax: Requires property, payroll and receipts from of a pass-through entity to be included in a taxpayer's apportionment formula in the same proportion by which the taxpayer shares federal taxable income or losses of the pass-through entity if such items were not excluded in computing taxable income or loss of the pass-through entity.

**SECTION 53:** Franchise and excise tax: Provides that the provisions of Sections 45 through 52 will take effect upon becoming law, which is June 28, 2000, and will apply to tax years ending on or after that date but will not take effect as

to any tax year in which an entity is not subject to franchise, excise taxes.

Pass-through entities, such as UP-REITs and QSSSs, that are newly created, and thus were not subject to franchise, excise taxes at the time Chapter 406 was enacted, do not come under the provisions of Sections 45 through 52 for a tax year in which the entity was not subject to franchise, excise taxes.

**SECTION 54:** Franchise and excise tax: Allows a credit against the total of franchise and excise taxes for the difference between property taxes associated with low income housing tax credit (LIHTC) property less the average property taxes projected for all LIHTC properties in the county in LIHTC program final applications filed prior to June 28, 2000 but after 1995. LIHTC property is defined as property participating in the IRS low income housing tax credit program on June 28, 2000. The amount of the credit must be determined each year, based on applicable property taxes. Any unused credit from one year may not be carried forward or backward to another year. For each LIHTC property, the credit may be taken in only five years, although not necessarily consecutively.

**SECTION 55:** Franchise and excise tax: A qualified business enterprise that makes a required capital investment in excess of 1 billion dollars resulting in at least 1,000 new full-time employee jobs in Tennessee is entitled to a credit of \$5,000 for each new job created. The investment must be made and the jobs created over a period not exceeding 3 years from the filing of the first related business plan. In order to qualify, the jobs must pay at least 150% of the average Tennessee industrial wage base

within 3 years (after initial training and experience).

**SECTION 56:** Franchise and excise tax: A qualified business enterprise that makes a required capital investment in excess of 500 million dollars resulting in at least 1000 new full-time employee jobs in Tennessee is entitled to a credit of \$5,000 for each new job created. The investment must be made and the jobs created over a period not exceeding 3 years from the filing of the first related business plan. In order to qualify, the jobs must pay at least 150% of the average Tennessee industrial wage base within 3 years (after initial training and experience).

**SECTION 57:** Franchise tax: Allows a taxpayer to exclude from its franchise tax minimum measure, two-thirds of all real and tangible personal property owned or used that was acquired as the result of job tax credit capital investments in excess of 1 billion or in excess of 500 million made in obtaining a \$5,000 per employee tax credit.

**SECTION 58:** Property tax: Establishes a local property tax exemption for a “family wellness center”. This tax is not administered by the Department of Revenue.

**SECTION 59:** Franchise and excise tax: Establishes a franchise, excise tax exemption for a family-owned entity that is not a corporation, where substantially all of its activity is production of passive investment income. For this purpose, the following is applicable:

- “Family Owned” means that at least 95% of the ownership units are owned by family members.

With respect to an individual only, this means:

An ancestor of the individual.

The spouse or former spouse of the individual.

A lineal descendent of the individual, his or her spouse or former spouse, or a parent of the individual;

The spouse or former spouse of the individual’s lineal descendent.

The estate or trust of a deceased individual who, while living, was any of the above.

- A legally adopted child of an individual is treated as his or her child by blood.
- “Passive investment income means gross receipts from royalties, rents, dividends, interest, annuities, and gains from sales or exchanges of stock or securities.

**SECTION 60:** Effective dates of the Act are as follows:

- Sections 1 through 38 take effect June 28, 2000, and apply to tax years beginning on or after July 1, 1999.
- With regard to LLCs, LLPs, and LPs that are directly or indirectly 80% or more

owned on or after June 30, 1998 by corporations subject to franchise, excise taxes under applicable statutes prior to their repeal by Chapter 406 of the Public Acts of 1999, Sections 1 through 38 are applicable to tax years ended on or after June 30, 1999.

- Section 43 of the Act takes effect January 1, 2001.
- All the remaining Sections of the Act take effect June 28, 2000.<sup>1</sup>

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Have questions or comments? Please let us know. [Contact us.](#)

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<sup>1</sup> Sections 45 through 52 took effect when the Act became law on June 28, 2000. However, Section 53 provides that such Sections are applicable to tax years ending on or after the effective date of the Act and will not apply to a tax year in which an entity was not subject to franchise, excise taxes.